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Rare win for customers in Hong Kong mis-selling case

The Court of First Instance in *Chang Pui Yin v Bank of Singapore Ltd* [2016] HKEC 1721 found in favour of two elderly customers who claimed they had been sold complex products which they did not understand and that were completely unsuitable for them. The judgment is in contrast to other recent cases and reflects a trend for courts (especially at first instance) to find a creative way around non-reliance language in banking contracts where the courts believe the merits favour the customer.

Overview

Although the language of the contracts was not clear-cut, the Court found the bank had a contractual duty to advise the customers and that the relationship was not an execution-only one.

Investing a windfall

The plaintiffs, Mr and Mrs Chang, were described as a simple elderly couple who led uncomplicated lives, until 1997, when Mr Chang received a large windfall of shares in a listed company and the proceeds of a property sale worth approximately HK$120 million.

Mr Chang gave away most of the money including US$1 million to his wife. The couple were introduced to Mrs Li, the relationship manager at their bank at their bank at the time, Standard Chartered Bank (SCB).

From 1997 to 2004, the Changs made only low to medium-risk investments at SCB, relying on the recommendations of Mrs Li to make good returns. In 2004, Mrs Li moved to the Bank of Singapore (the Bank) and the Changs followed her, opening accounts there.

From that point on they started purchasing large amounts of high-risk investments, such as equity-linked notes, foreign currency options, knock out daily accumulators, high yield bonds and equity options.

The Court found that that the Changs had no more than a very basic understanding of the products they were being sold. The Court accepted their evidence that their investment objective had always been to preserve their capital and achieve a return that was slightly better than bank deposits.

The Court found that Mrs Li never said anything to them about risk or explained the features of the products yet continually assured Mrs Chang they had nothing to worry about.

The documentation

The Court considered whether the key agreements were *"execution only"* or whether they contained an advisory element. The primary clause governing the scope of the banking services being provided read in part:

" Investments will be as directed by you in the case of custody Accounts (Custody Accounts) and Accounts which are established on an advisory

Key issues

- The Court found the bank had a contractual duty to advise the customers and that the relationship was not an execution-only one.
- The Bank had breached the duty by offering products that were unsuitable for them and not warning them of the risks.
- With the SFC introducing a new suitability requirement into client contracts, it will be important for banks to carefully document their suitability obligations as a defence against future mis-selling claims.

basis only (Non-Discretionary Accounts)."

The Court found that *"to suggest that 'advisory basis' means 'advise'* (sic) *or 'notice' from the client as to what to buy or sell does not sit well with the first part of the sentence which already states that investments will be directed by the client".*

The term *"advise"* also often implied professional or technical expertise. The expression *"established on an advisory basis only"* suggested the Bank was providing an advisory service.

The Court therefore distinguished this case from earlier cases such as *DBS Bank (Hong Kong) Ltd v San-Hot HK Industrial Co Ltd* [2013] 4 HKC1 and *Kwok Wai Hing Selina v HSBC Private Bank (Suisse) SA* [2012] 4 HKC 260 which had resulted in wins for the banks, as these had been concerned with *"execution only"* banking services.

There were no provisions in the key agreements that defined the scope of the Bank's duty to provide advice to clients who opened a non-discretionary account on an advisory basis only.

The Court relied on an earlier case of *Susan Field v Barber Asia Ltd* HCA 7119/2000, to find that Mrs Li and the Bank breached a contractual duty of care owed to the customer by failing to exercise reasonable care and skill: (i) in ascertaining and having regard to the Changs' investment objectives and risk appetite; (ii) by offering products which were not suitable for their investment objectives and risk appetite and (iii) by not warning of the risks inherent in the investments that were being offered to them.

Contractual Estoppel

The Court held that, if it was wrong and the contract was *"non-advisory"* and *"execution only"*, then the Bank would have succeeded in its defence of contractual estoppel. The contractual terms as stated would have catered for that situation and would have absolved the Bank from liability.

The Court rejected counsel's submissions that the doctrine itself was not properly founded in law, citing the Court of Appeal's observations in *DBS (Hong Kong) Ltd v Sit Pan Jit* CACV 91 of 2015[1]

Control of Exemption Clauses Ordinance

The Court noted that if the contracts were execution only and not advisory, the plaintiffs could not seek relief under the Control of Exemption Clauses Ordinance, Cap. 71 (CECO).

The Court said there was a clear distinction between clauses which exclude liability, and clauses which define the terms upon which the parties are conducting their business. CECO applied only to the former.

The terms of the risk disclosure statements in the present case were similar to the clauses in question in *DBS Bank (Hong Kong) Ltd v San-Hot HK Industrial Co Ltd* [2013] 4 HKC 1.[2] It would have been reasonable for the Bank to contract on the basis it was providing an "*execution-only"* service, and the clauses concerned would not have fallen foul of CECO.

Suitability Requirement

The trial judge, Bharwaney J, distinguished the facts in this case from other recent mis-selling cases.

"In all these mis-selling cases, private banking relationship managers rightly complain that their clients accuse them of wrongdoing when markets fall and forget about all the profits they accumulated when times were good. Such clients deserve no sympathy.

They knew the risks involved and took them with eyes wide open. They took huge bets and, when markets were favourable, enjoyed amazing returns on their investments. When markets went south they employed smart lawyers to look for loopholes in the banking documentation in order to sue their private bankers.

The Changs are wholly different from the vast majority of plaintiffs pursuing their private bankers in our courts. The Changs were elderly, unsophisticated clients to whom Mrs Li was keen to sell investment products which they little understood."

The courts' efforts to find justice for unsophisticated clients such as the Changs has been given a boost by the SFC which, in December 2015, introduced a change to the Professional Investor Regime, requiring financial intermediaries to include a clause in client agreements ensuring that any financial product solicited for sale or recommended to a client is reasonably suitable for the client, regardless of what may be stated elsewhere in the client agreement.

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[1] Clifford Chance Client Briefing June 2016 – *"Hong Kong Court of Appeal confirms win for bank in mis-selling case"*

[2] Clifford Chance Client Briefing March 2013 – *"Hong Kong court again places reliance on contractual terms to dismiss mis-selling claim against private bank"*

The clause will enable investors to claim for damages under the client agreement where an intermediary sells or recommends products that are not reasonably suitable for a particular customer.

Although there is a long-stop date of June 2017 for the clause to be included, the SFC has made it clear it expects banks and financial intermediaries to start including the clause in their contracts straight away.

The effect is that banks and financial intermediaries will no longer be able to point to a non-reliance clause to create a contractual estoppel and limit the duties owed to the customer.

As such, it will become even more important for banks and financial intermediaries to observe and carefully document their suitability obligations as a defence against future mis-selling claims.

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